

Appeal of Bondholders¹ Committee of
the San Joaquin Agricultural Corporation

"rights and powers of the owners and/or holders of all bonds deposited" with the express power to purchase the property security and to sell, lease and exchange it. The Committee was not authorized to reinvest the proceeds from the sale of the property, or any portion thereof, but was rather required to distribute the proceeds of any such sale or any other income from the property to the depositors of the bonds.

The proposed assessments for the income years 1935, 1937, and 1938 were based on the definition of business trust set forth in Section 3 of the Massachusetts or Business Trust Tax Act as follows:

"The term Massachusetts or business trust as herein used shall include every business organization consisting essentially of an arrangement whereby property is conveyed to trustees where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries but are associated together with similar or greater powers than directors in a corporation for the purpose of carrying on some business enterprise."

For the taxable years 1939 and 1940, the proposed assessments were made pursuant to the Corporation Income Tax Act. Section 2(b) of this act provides that the term "corporation" shall include associations and Massachusetts or business trusts, which are defined as follows:

"For the purposes of this act a Massachusetts or business trust includes every business organization consisting essentially of an arrangement whereby property is conveyed to one, or more than one, trustee for purposes other than the mere conservation of assets, collection and disbursing of fixed and periodic income, or the securing of an obligation."

The, only question at issue is the taxability of the Appellant as a business organization within the meaning of these definitions.

The rules applied by the Federal courts in determining whether similar organizations are taxable as associations classified as corporations under Section 3797 of the Internal Revenue Code are pertinent here. Koenig v. Johnson, 71 Cal. App. 2d 739. These rules are summarized in the leading case of Morrissey v. Commissioner of Internal Revenue 296 U. S. 344, wherein it was held that the basic tests to be applied to an association to determine its taxability as a corporation are whether the organization consists of associates in a joint enterprise, whether it is an enterprise for the transaction of business, and whether there is resemblance to a corporate entity. Mere liquidation, in the course of which are conducted only such activities as are incidental or necessary thereto, frequently has been held, however, not to constitute the transaction of business. White v.

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Hornblower, 27 Fed. 2d 777; Helvering v. Washburn, 99 Fed. 2d 478; Paine v. United States, 32 F. Supp. 672; Myers v. Commissioner of Internal Revenue, 89 Fed. 2d 86. Our inquiry is directed, accordingly, to ascertainment of whether the dominant purpose and actual activities of Appellant involved merely the liquidation of its property.

It is clearly established by the record that Appellant engaged in no business activity other than that essential to the liquidation of its real property. The reservation of mineral rights in the deeds of the property sold, although it might possibly have put the Appellant in a position to engage in business in the future, did not have that effect during the years here in question.

The Commissioner contends, however, that the agreement gave the Committee power to engage in business and, quoting from Helvering v. Coleman - Gilbert Associates, 296 U. S. 369, 374, he states that "the parties are not at liberty to say that their purpose was other or narrower than that which they **formally** set forth in the instrument under which their activities were **conducted.**" See also Sears v. Hassett, 111 Fed. 2d 961; Jackson v. United States, 110 Fed. 2d 574. Although the agreement not provide in so many words that the primary purpose of the bondholders' committee was the liquidation of the property security, when the agreement is read as a whole it seems clear that this was the dominant purpose and that any other powers conferred were only incidental to this purpose. Persuasive evidence of this purpose is to be found in the provision of the agreement requiring the distribution to the depositing bondholders of any proceeds from the sale of the property. The situation presented in the instant case is, accordingly, readily distinguishable from those involved in the authorities above cited, wherein it was determined that the primary purpose of the bondholders' committee or trust was the carrying on of business and that the liquidation of the property was only incidental. Moreover, considerable stress was put therein on the business activities actually carried on by the committee or trustees while here the Appellant engaged in no other business than that incidental to liquidation of the property security.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED that the action of Chas. J. McColgan, Franchise Tax Commissioner, in overruling the protests of the Bondholders' Committee of the San Joaquin Agricultural Corporation to proposed assessments of additional tax in the amounts of \$38.57, \$129.33 and \$158.70 for the income years 1935, 1937 and 1938, respectively, pursuant to Chapter 211, Statutes of 1933, as amended, and in the amounts of \$152.99 and \$141.11 for the taxable years 1939 and 1940, respectively, pursu-

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ant to Chapter 765, Statutes of 1937, as amended; be and the same is hereby reversed. Said ruling is hereby set aside and the Commissioner is hereby directed to proceed in conformity with this order.

Done at Sacramento, California, this 1st day of November, 1946, by the State Board of Equalization.

Wm. G. Bonelli, Member
J. H. Quinn, Member
Thomas H. Kuchel, Member
George R. Reilly, Member

ATTEST: Dixwell L. Pierce, Secretary